

CALIFORNIA GAMBLING CONTROL COMMISSION
LEGAL DIVISION MEMORANDUM



Public Staff Report for March 27, 2008 Commission Meeting

Date: March 21, 2008
To: Commissioners
Copy: Steven V. Giorgi, Executive Director
From: Heather Cline Hoganson, Staff Counsel
Cyrus J. Rickards, Chief Counsel
Subject: Proposed Tribal Regulation (Compact Sections 8.4, 8.4.1) - CGCC-8

Recommendation:

APPROVE the attached regulatory text (dated March 13, 2008) to be forwarded to the Tribal-State Regulatory Association (Association) for consideration at the May 7, 2008 Association meeting.

Summary:

The Tribal-State Gaming Compact (Compact) empowers the State, through its State Gaming Agency (SGA), to conduct compliance reviews of various aspects of each Tribe's Class III gaming operation.¹ Compact Sections 8.4 and 8.4.1 provide a process for the establishment and adoption of regulations by the SGA. This proposed regulation (CGCC-8) is designed to establish a process for the exercise of the SGA responsibility of ensuring compliance with the Compact's requirements that the Tribal Gaming Agency assume the primary role in establishing and enforcing rules, regulations, procedures, and specifications regarding the Class III gaming operation. In order to meet the goal of statewide uniformity of regulation of Class III gaming expressed in Compact Section 8.4, this regulation (CGCC-8) incorporates the National Indian Gaming Commission's Minimum Internal Control Standards (NIGC MICS) as baseline minimum standards for California Class III gaming.

Background:

1. Regulatory Process

In the Spring of 2007, California Gambling Control Commission (Commission) staff presented the concept of CGCC-8 to the Association. A draft was presented to the Association in July 2007, and a Task Force was appointed to review the proposal, in accordance with the Protocol for Submission of Proposed State Regulatory Standards to the Association (Protocol).

¹ Under the Compact, Tribes are authorized to conduct the following Class III gaming activities: gaming devices, banking or percentage card games, and devices that are authorized under state law to the California State Lottery. (See Compact Section 4.0.)

The Task Force met August 8, 2007, September 11, 2007, November 7, 2007, January 9, 2008, and February 13, 2008. The Commission was given alternative language by members of the Task Force, but not by the Task Force itself. The Task Force (minus State Gaming Agency representatives) issued a Final Report on February 13, 2008.

At the noticed meeting of the Commission on February 21, 2008, the Commissioners received oral comments on draft CGCC-8. Staff has incorporated many of the language suggestions received and is presenting a final draft proposal for adoption by the Commission. If adopted, the text will then be forwarded for consideration by the Association at its May 7, 2008, meeting, pursuant to Section 8.4.1 of the Compact. That meeting will constitute the “initial” reading of the text under the Protocol.

Pursuant to the Protocol, at the initial meeting at which a proposed regulation is presented for consideration, no vote may be taken². At least one additional meeting shall be conducted no less than 30 days nor more than 90 days after the initial meeting, at which time the proposed regulation shall be voted upon³. One 30-day extension may be granted beyond the 90 days, upon a majority vote of the Delegates present at an Association meeting.⁴ Unless the SGA withdraws the proposed regulation, or notice is not properly provided, a vote shall be taken by the Association.⁵

If the proposed regulation is approved by the Association, it must then be submitted to the Tribes for comment. The Commission must consider any comments before final adoption.⁶ If the proposed regulation is disapproved, it shall not be submitted to the Tribes for comment unless it is re-adopted by the SGA, with a detailed, written response to the Association’s objections.⁶

2. Tribal Regulation and State Compliance Oversight

Gaming is the quintessential cash business and internal controls are the primary procedures used to protect the integrity of casino funds and games. Internal controls are therefore a vitally important part of properly regulated gambling.

In California, the Compact places primary responsibility for the establishment and enforcement of internal controls regarding Class III gaming with the Tribal Gaming Associations (TGAs). The Compact requires Tribes to adopt gaming ordinances. It further requires TGAs to adopt internal rules, regulations, and specifications (control standards) regarding specific aspects of the gaming operation and to ensure that the gaming operation is conducted according to those standards.⁷ Nevertheless, the Compact also makes clear that the SGA has the right to inspect the Gaming Facility and all Gaming Operation or Facility records with respect to Class III gaming to ensure Compact Compliance.⁸

² Protocol, section C 2(a). See *also*, Section 8.4.1(c) of the compacts.

³ Protocol, section C 2(b).

⁴ Protocol, section C 2(e)(3).

⁵ Protocol, section C 3.

⁶ Section 8.4.1(b) of the compacts.

⁷ See Compact Sections 6.1, 7.1, 8.1 and following.

⁸ See Compact Sections 7.4, and following.

CGCC-8 is designed to facilitate the State's exercise of its compliance responsibilities under the Compact. It provides a process for accomplishing compliance oversight, including a process for dispute resolution between the Tribe and the SGA prior to either the State or the Tribe moving to the Compact's dispute resolution process. CGCC-8 also includes the NIGC MICS as a baseline for tribal internal controls.

The NIGC MICS were designed to establish a baseline, that is MINIMUM internal control standards, to be required of tribal gaming operations. Initially adopted in January 1999 (before the original Tribal-State Gaming Compacts were negotiated in California), and designed with substantial input from gaming tribes, the NIGC MICS have been amended over the years to take into account advances in technology, and to clarify certain requirements. Amendments were based on input by NIGC auditors and field staff, tribal gaming representatives, and the public at large.⁹

The NIGC MICS are structured by size of gaming operations rather than by type of game (Class II or Class III). This recognizes that the requirements placed upon Tribal gaming operations should differ based upon their annual gross gaming revenue. CGCC-8 establishes the NIGC MICS solely as a baseline. The regulation does not require that any Tribe adopt the NIGC MICS, but only that the Tribe's own internal control standards equal or exceed the NIGC MICS. This standard was chosen because most, if not all, gaming Tribes, already use the NIGC MICS as a baseline and, as such, it is the industry standard for Tribal gaming in California.

Conclusion:

CGCC-8 is an attempt to cooperatively establish uniform protocols and standards for State compliance review of Class III gaming operations. It attempts this by establishing the NIGC MICS as a baseline for Tribal gaming operations and by establishing procedural rules for State oversight of compact compliance. Using the NIGC MICS as a baseline standard ensures consistency and uniformity while taking into account the size of gaming operations. Further, since the Tribes have been using this standard for years, this approach eliminates duplication or unnecessary promulgation of new rules, regulations, or specifications. Since the State already has significant oversight authority expressed in the compacts, CGCC-8 would not constitute an expansion of that authority, but would be a method of facilitating the exercise of that authority.

This final proposed draft integrates many of the ideas, criticisms, and suggested language expressed during the lengthy Task Force process outlined above. Staff believes it clearly preserves the primary role of Tribal Gaming Agencies in the regulation of Class III gaming under the Compact, while establishing a rational process for the State to exercise its clear authority to ensure compact compliance. This regulation respects Tribal sovereignty while at the same time ensuring that the State, in its sovereign role as a Compact signatory and pursuant to specific Compact language, may assure its citizens that it is exercising its role to ensure Compact compliance in the regulation of Class III gaming.

Document Attached:

- Proposed Uniform Tribal Gaming Regulation CGCC-8 (MICS) (dated March 13, 2008).

⁹ According to the NIGC, they have conducted 6 to 8 full, on-site compliance audits in California from 2000 to 2006.

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Minimum Internal Control Standards

Table of Contents:

- (a) Purpose.
- (b) Internal Control Standards.
- (c) Internal Control System.
- (d) Net Win.
- (e) Financial Statements Audit.
- (f) Agreed-Upon Procedures Audit.
- (g) State Gaming Agency Access to Records.
- (h) CGCC Review of Independent Audits.
- (i) CGCC Report Acceptance and Tribal Action Plan.
- (j) CGCC Compliance Review Report Dispute.
- (k) Confidentiality.
- (l) Variance to Internal Control Standards.
- (m) Updating Internal Controls and this Regulation.
- (n) Disputes.

(a) Purpose. The Tribal-State Indian Gaming Compact (Compact) empowers the State, through its State Gaming Agency (SGA), to conduct compliance reviews of various aspects of each Tribe's Class III Gaming Operations. Specifically, Section 6.0 of the 1999 Compact, and comparable sections of new or amended Compacts, provide that each Tribe will conduct its Gaming Operation in compliance with a Gaming Ordinance adopted by the Tribe, and rules, regulations, procedures, specifications and standards adopted by the Tribal Gaming Agency (TGA). Section 8.1 of the 1999 Compact, and comparable sections of new or amended Compacts, charge the TGA with responsibility to promulgate such rules, regulations and specifications and to ensure their enforcement. Compact sections 8.1.1 through 8.1.14 outline the matters which, at a minimum, these rules, regulations, and specifications must address. Compact sections 7.4 through 7.4.4 provide the State Gaming Agency the authority to inspect the Gaming Facility, as defined in the Compact, as reasonably necessary to ensure compliance with the Compact. The purpose of this regulation is to

1 provide an effective uniform manner in which the SGA can conduct compliance
2 reviews of the adoption and enforcement of these rules, regulations, and
3 specifications by the TGA, and to protect the public as well as each Tribe. As
4 defined in Section 2.18 of the Compact, the State Gaming Agency includes the
5 California Gambling Control Commission (CGCC) and the Department of
6 Justice, Bureau of Gambling Control (Department). Nothing in this regulation
7 shall modify or otherwise affect the rights and obligations of the SGA under the
8 Compact, including but not limited to, the SGA entities' ability to share
9 documents provided pursuant to this regulation, subject to the Compact's
10 confidentiality provisions.
11

12 (b) Internal Control Standards. Each Tribal Gaming Agency (TGA) shall maintain
13 written internal control standards applying to its operation and support of Class III
14 gaming that equal or exceed the Minimum Internal Control Standards (MICS) set
15 forth at 25 CFR Part 542 (as in effect on October 1, 2006, as may be amended
16 from time-to-time), and shall provide a copy of these standards to the CGCC staff
17 within 30 days of the effective date of this regulation. Copies of any amendments
18 to these standards shall be provided to the CGCC staff within 30 days of adoption
19 by the TGA.
20

21 (c) Internal Control System. Each Tribe shall implement and maintain an internal
22 control system that, at a minimum, ensures compliance with the tribal internal
23 control standards that apply to its operation and support of Class III gaming.
24

25 (d) Net Win. The definition of "net win" contained in the applicable Tribal-State
26 Compact shall apply to matters covered by this regulation, rather than the
27 definition of "net win" provided at 25 CFR 542.19(d).
28

1 (e) Financial Statements Audit. Section 8.1.8 of the 1999 Compact, and comparable
2 sections of new or amended compacts, provide that each Tribe shall engage an
3 independent Certified Public Accountant (CPA) to provide an annual audit of the
4 financial statements of each Gaming Operation. Such financial statements shall
5 be prepared in accordance with generally accepted accounting principles and
6 financial statements audits shall be conducted in accordance with generally
7 accepted auditing standards, as supplemented by the standards for audit of casinos
8 of the American Institute of Certified Public Accountants. Each Tribe shall
9 submit to the CGCC staff all audit report information, including management
10 letters and responses to management letters, pertaining to the operation and
11 support of Class III gaming, within 120 days after the completion of the audit.
12 The Tribe may elect to provide the entire audit report to the CGCC staff for
13 review and CGCC staff will only utilize or record those aspects affecting the
14 operations and support of Class III gaming.

15
16 (f) Agreed-Upon Procedures Audit. Each Tribe shall engage an independent CPA to
17 perform an annual "Agreed-Upon Procedures" audit in accordance with 25 CFR
18 542.3(f) to verify that the gaming operation is in compliance with the Tribe's
19 written internal control standards. Either the firm or all independent certified
20 accountants engaged to perform an "Agreed-Upon-Procedures" audit must be
21 licensed by the California Board of Accountancy. The CPA shall prepare a report
22 of the findings for the Tribe. The Tribe shall submit a copy of the report to the
23 CGCC staff no later than 120 days after the completion of the audit.

24
25 (g) State Gaming Agency Access to Records. Pursuant to Section 7.4 and following
26 of the 1999 Compact, or comparable sections of new or amended Compacts, SGA
27 staff shall be given prompt access to all gaming operation facilities, equipment,
28 personnel, and records reasonably necessary to ensure compliance with the
29 Compact. Tribal officials shall not unreasonably withhold or deny access to

1 records deemed necessary for compliance review by SGA staff. Upon request
2 and notice to the Tribe and the TGA, the SGA staff shall be granted access during
3 normal hours of the Gaming Facility's business office for inspection and copying
4 records of the operation and support of all Class III gaming, including, but not
5 limited to: internal control standards; work-papers of the independent CPA
6 generated in performing the Agreed-Upon-Procedures audit; reports and work
7 papers of the internal audit staff; observation checklists; CPA MICS compliance
8 checklists or other comparable testing procedures; findings by the independent
9 CPA or the internal audit staff; and exceptions and gaming operation response to
10 the exceptions. The TGA and the Tribe shall permit the SGA staff to interview
11 and consult with the independent CPA before and after the performance of the
12 Agreed-Upon-Procedures audit.

13
14 (h) CGCC Review of Independent Audits. CGCC staff shall review both the audit of
15 the financial statements pertaining to the operation and support of Class III
16 gaming, the Agreed-Upon-Procedures report, and all information supplied by the
17 Tribe and the TGA and may choose to conduct on-site compliance reviews of the
18 operation and support of all Class III gaming. The compliance reviews
19 authorized by this regulation shall not be construed to authorize the State to
20 conduct a full financial audit as is required of the Tribe by Section 8.1.8 of the
21 1999 Compact or authorized pursuant to 25 CFR 571.12.

22
23 (i) CGCC Report Acceptance and Tribal Action Plan. If an on-site compliance
24 review is conducted, CGCC staff shall provide a draft Compliance Review Report
25 (Report) to the Tribe and to the TGA, including findings of non-compliance, if
26 any. The Tribe shall have 60 days, or such other time period as is mutually
27 agreeable, to respond to the CGCC draft Report. If the Tribe accepts the draft
28 Report, CGCC staff shall finalize its Report and, within 20 days of acceptance,
29 submit the final Report to the Tribe and the TGA. Within 45 days of receipt of

1 the final Report, the Tribe shall acknowledge the Report and, if findings require,
2 provide a written action plan including proposed time line addressing the
3 findings. CGCC staff may review the impact or implementation of any action
4 plan undertaken by the Tribe pursuant to this regulation and may issue an Action
5 Plan Assessment to the Tribe.

6
7 (j) CGCC Compliance Review Report Dispute. If, after a 60-day review, the Tribe
8 contests the draft Report, CGCC staff and the Tribe shall make good faith efforts
9 to resolve any differences. Upon notice by the Tribe of a disagreement and
10 failure to resolve differences, the CGCC staff will finalize and deliver the Report.
11 Within 30 days of receipt, the Tribe shall provide a written explanation of its
12 reasons for disputing the findings. The Report and the Tribe's explanation of the
13 dispute shall be referred for consideration by the full CGCC. At the request of the
14 Tribe, the matter may be set for closed session consideration at which time the
15 Tribe may offer any evidence to support its position and/or offer a compromise
16 reconciliation. All information presented shall be subject to the confidentiality
17 provisions of the Compact. If, after consideration and decision by the full CGCC,
18 a dispute remains, it may be resolved pursuant to the dispute resolution process
19 outlined in Compact Section 9.0.

20
21 (k) Confidentiality. Pursuant to Compact section 7.4.3(b), or comparable sections of
22 new or amended Compacts, the SGA shall exercise utmost care in the
23 preservation of the confidentiality of any and all information received from the
24 Tribe in compliance with this regulation, including but not limited to tribal
25 internal control standards, third-party audits, tribal audits, and state compliance
26 reviews, and shall apply the highest standards of confidentiality expected under
27 state law to preserve such documents from disclosure.

1 (l) Variance to Internal Control Standards. A TGA may approve a variance from the
2 control standards set out at 25 CFR Part 542, following the procedure outlined in
3 25 CFR 542.18(a). The other procedures found at 25 CFR 542.18(a) through (e)
4 shall also apply to variances sought under this regulation, except that the review
5 of the TGA approval shall be conducted by the Chairperson of the CGCC and the
6 TGA shall be entitled to an appeal to the full CGCC in the event that the
7 Chairperson files objections to a re-submission of a variance as provided in 25
8 CFR 542.18(d).

9
10 (m) Updating Internal Controls and this Regulation.

- 11 (1) Nothing in this regulation shall be construed to preclude individual tribes
12 and the SGA from meeting, from time-to-time, to discuss MICS
13 compliance matters in light of changing technology or industry best
14 practices.
- 15 (2) The Tribal-State Regulatory Association may meet from time-to time, but
16 not less often than once every two years, to discuss possible modifications
17 of this regulation in light of changing technology or industry best practices.

18
19 (n) Disputes. If a dispute not previously addressed by this regulation arises between
20 CGCC staff and a Tribe involving the application or interpretation of this
21 regulation, the following procedure shall be followed:

- 22 (1) The parties shall make good faith efforts to resolve their differences.
- 23 (2) If these good faith discussions do not resolve the matter, then the matter
24 shall be referred to the full CGCC for review and decision. At the request
25 of the Tribe, the matter may be set for closed session consideration.
- 26 (3) After the full CGCC reviews the matter and makes a decision, or if the full
27 CGCC for any reason does not make a decision, the Tribe shall be entitled
28 to invoke the dispute resolution process outlined in Compact section 9.0.
- 29 (4) If the Tribe declines to follow the decision of the full CGCC, the State
30 shall be entitled to invoke the dispute resolution process outlined in
31 Compact section 9.0.